

OPENNESS, INSTITUTIONS AND FINANCIAL DEVELOPMENT IN ECOWAS COUNTRIES

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Abstract

There exist a vast literature in support of the positive link between financial development and economic growth in many countries. The question of what drives financial development within the Economic Community of West African States (ECOWAS) as a group, is however not conclusively addressed by the extant literature. This study sheds light on the relationship by examining the role of openness and institutions in the financial development of ECOWAS countries. The hypothesized link between openness, institutions and financial development was specified in a linear dynamic panel data model and estimated using system generalized methods of moment (SGMM). The study found a positive and statistically significant link between openness and financial development while institutions contribute negatively to financial development in the region over the study period. The negative link between institutions and financial development may be indicative of the weak institutions within the region. The study supports the promotion of trade and financial openness as well as strengthening institutions to promote financial development in ECOWAS.

Keywords: *Openness, Institutions, Financial Development, System Generalized Methods of Moment (SGMM).*

INTRODUCTION

Despite the glaring importance of financial development to any economy, many economies in Africa remained financially underdeveloped. Evidence from prior studies as well as several indicators of financial development in Africa suggests that the continent lags behind in terms of financial development. In fact, as Mlachila *et al.* (2010); suggest that a look at the development of the financial sector over time reveals that financial depth has increased in sub-Saharan Africa but has generally not caught up with that of other developing countries; also a look at the Domestic credit to private sector (% of GDP) shows financial development in other regions of the world is much faster than it is in the Economic Community of West African States (ECOWAS) region.

Switzerland for instance, experienced improved financial deepening (domestic credit to private sector as % of GDP) from 95.9 percent in 1960 to 98.45 percent in 1970 which grew further to 148.9 and 158.6 percent in 1990 and 2010 respectively. It increased further to 174.1 percent in 2015. Most developing



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countries on the other hand, experienced very slow development of their financial sector during the same period. In fact, a few countries in ECOWAS show a slow increase in financial development. For example, Ghana with financial deepening of 4.5 percent in 1960 grew to 8.2 percent in 1970, but fell to 2.1 percent in 1980 and then grew again to 4.9 percent in 1990 (WDI, 2016). The country recorded 13.9 percent in year 2000 and this increased further to 15.2 percent in 2010 and 20.2 percent in 2015. For Senegal, it was 14.8 percent in 1960 but fell to 13.2 percent in 1970, increased to 36.4 percent in 1990 and declined to 2.2 percent in 2000, this again increased to 25.7 and 33.5 percent in 2010 as well as in 2015. In the case of Nigeria, financial deepening was 3.6 percent in 1960, 4.9 percent in 1970, 12.25 in 1980 and 8.7 percent in 2010 and this rose to 15.4 percent in 2015 (WDI, 2016).

Evidence from both theoretical and empirical researches confirms the existence of links between trade openness and financial development especially in developing countries (Do & Levchenko, 2004). Also the role of institutions in influencing financial development has received a lot of attention in the literature especially in recent times. Demitriades and Andrianaonova (2004) argue that the strength of institutions such as financial regulation and the rule of law may determine the success or failure of financial reforms. Law, Hook and Azman-Saini (2008) using banking sector and stock market development indicators explored the importance of a wide range of institutional quality variables as sources of financial development, concluded that a high quality institutional environment has positive effect on financial development. Similarly, it is clear from the literature that strong institutions promote financial development and that openness in both trade and finance drive financial development. Therefore, Baltagi *et al.*, (2009) established that openness and economic institutions can explain a large part of the variation in financial development across countries.

It is however unclear why there is dearth of literature that attempts to explain the low level of financial development in ECOWAS countries. Therefore, this paper evaluates the plausible effect of openness and institutions on financial development in ECOWAS region. Specifically, the objectives include whether strengthening institutions would improve financial development in the region or whether trade and financial openness are enough to improve financial development without strengthening institutions in ECOWAS. The paper is structured into six (6) sections; the introduction, literature review, stylized facts, methodology, discussion of results and conclusions.

LITERATURE REVIEW

Trade openness and trade liberalization are interchangeably used in literature. Trade liberalization includes policy measures to raise trade openness while increased trade openness is usually considered as an increase in the size of a country's traded sectors in relation to total output. Increased openness can, but need not, be the result of trade liberalization. Recently, the meaning of "openness" has become identical to the idea of "free trade" that is a system where all trade distortions are eradicated (Balanika, 2009).

Institutional quality on the other hand is the extent to which man-made procedures foster investor protection and enhance access to funds for entrepreneurs within financial exchanges (Herger, Hodler &



Onoja *et al.*

Lobsiger, 2007). According to Institutions theorists, upholding and credibly enforcing property rights (i.e. the right of property owners to extract returns on investment) stands crucial in financial transactions since potential financiers will be reluctant to surrender funds in the face of risks of being expropriated. In other words, investors rely on the state for enforcing contracts and protection. Hence, in countries where corrupt politicians/official abuse their authority for self-enrichment, investors would be unwilling to invest or surrender funds with increasing risks of expropriation, explaining why these states remain financially under-developed.

Financial integration involves a process whereby a country's financial markets become linked or integrated with those of other countries or with those of the rest of the world. In fully integrated markets, all forms of barriers are eliminated to enable foreign financial institutions to participate in domestic markets. In such an environment, domestic banking networks, equity and other types of financial markets are linked to their foreign counterparts.

Patrick (1966) took a lead from Goldsmith's analysis to formulate the demand-following and supply-leading hypothesis to explain the causal nature of the relationship between financial development and economic growth. In his words, "the causal nature of this relationship between financial development and economic growth has not been fully explored either theoretically or empirically". The author asserts that the transition from a traditional/neo-classical state equilibrium analysis to a more advanced/developed financial system which comprises financial intermediaries leads to a 'demand-following' phenomena.

On the hand, the McKinnon and Shaw (1973) model showed that the relationship between financial deepening and economic development is based on the complementarity between money and capital. In this model, a positive real interest rate increases financial deepening via the mobilization of an increased volume of savings and promotes growth through a higher productivity of capital. McKinnon and Shaw in their hypothesis assert a positive relationship between interest rate and financial deepening. They said developing countries have repressed economies with ceilings on interest rates and limitations in credit availability which imposes restrictions on growth. Adebisi (2003) re-examines McKinnon-Shaw hypothesis on money demand function for seven African Less Developed Countries (LDCs). The findings of the study support the assertion that the conditions necessary for complementarity are characteristics of the world's least developed economies.

Fenira (2015) demonstrates the effect of trade openness on economic growth in 82 developing countries. The study employed Panel Least Square with dummy variables and comparative analysis of trade indexes using annual data from 1996 to 2012. The study found that trade policy liberalization has weakly contributed in improving economic growth in these countries. Also, Elie (2015) evaluated financial development and economic growth in Sub-Saharan Africa countries using dynamic panel GMM technique of annual data from 2000 to 2014. The study found a strong positive causal relationship between financial sector development and the growth of the economies of Sub-Saharan economies.



Onoja *et al.*

Menyaha, *et al.*, (2014) examines the causal relationship between financial development and economic growth for 21 African countries within a framework which also accounts for international trade. They developed a financial development index based on four different financial development indicators and apply the panel bootstrapped approach to Granger causality. The empirical results show limited support for the finance-led growth and the trade-led growth hypotheses. The results imply that recent attempts at financial development and trade liberalization do not seem to have made a significant impact on growth.

Antonio, Montfort and Ashwin (2014) analyze the plausible link between financial and trade openness, and financial development in 34 Sub-Saharan African (SSA) countries from 1970 to 2009. They employed Common Correlated Effects (CCEMG) estimator to control for the problems of cross-sectional dependence. The study couldn't find any direct link between trade openness and financial development in SSA due largely to distortions in domestic financial markets, relatively weak institutions and poor financial supervision. Also, Asiama and Mobolaji (2011) investigated the interactions between trade and financial openness, institutional quality, and financial development in Sub-Sahara Africa (SSA) countries. The study employed panel data from 33 SSA countries over the period of 6 years from 2004 to 2009. The econometrics technique used includes Arellano and Bond (1991) dynamic panel data estimator (DPD) based on the Generalized Methods of Moments (GMM) technique. They found that broad money supply as a measure of financial development exhibits positive statistically insignificant impact on trade openness.

Karikari (2010) evaluate the roles of governance and financial liberalization in the financial development of 37 Sub-Saharan Africa (SSA) countries yields several interesting results using data from 1996 to 2008. The study employed Panel regression with governance index as an independent variable. The paper revealed that from 1996 to 2002, the impact of financial liberalization was reduced with good governance, probably due to governments' forbearance of weak state-owned banks; but, since 2003 good governance has increased the impact of financial liberalization on financial development.

One thing coming out clearly from the studies reviewed is the mixed nature of results in spite of the fact that they all employed panel data. It will only be appropriate therefore to remark that results from these studies are largely inconclusive emphasizing the need for further studies to provide additional insights.

SOME STYLISED FACTS

The stylized facts show trends in the various macroeconomic and institutional variables observed over time. These key macroeconomic variables include: trade openness and financial development, while the institutional quality measures include: Regulatory Quality (RQ), Rule of Law (RL) and Control of Corruption (CC). The trend analysis was carried out on four countries with the highest financial development score from 1996 to 2015. The countries include Cape Verde, Ghana, Nigeria and Togo. Private sector credits as ratio of gross domestic product was used as a measure of financial development.



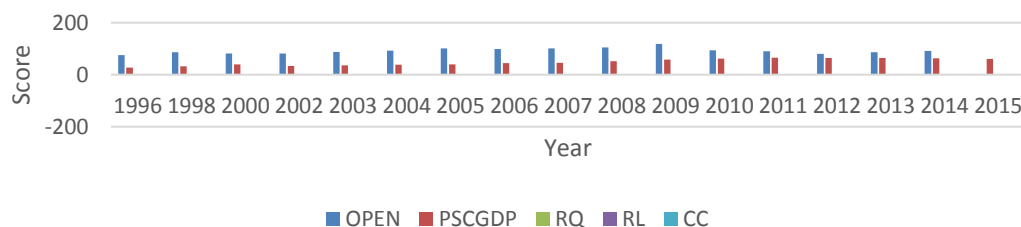
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Onoja et al.

**Figure 1: Trend of selected
macroeconomic and
institutional variables for Cape Verde**



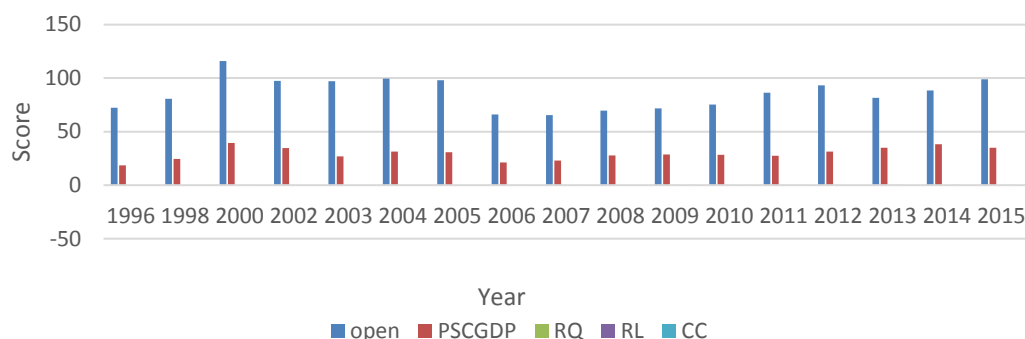
Source: Authors' computation using data from WDI and WGI (2015)

Available data indicate that Cape Verde is the most financially developed among the selected countries followed by Ghana, Nigeria and Togo. The evidence also suggests that Cape Verde had the strongest institutions in terms of regulatory quality and control of corruption while Ghana had the strongest rule of law in 2015. Some of the reasons for these could be that democratic process in Cape Verde had been relatively peaceful and stable with free and fair electoral processes as well as free press (International Peace Institute, 2011). Also, the nation had experienced ten peaceful presidential and legislative elections since 1991 (International Peace Institute, 2011). For all the years under review, it can be observed that the various macro-economic variables are in the positive region; between 2002 to 2011 credit to private sector registered an upward trend and stabilized thereafter till 2014 before dropping slightly in 2015. This observed trend is similar for trade openness, which peaked in 2009 before experiencing some decline in the following years. The institutional variables were also in the positive region throughout the years under review; this is however with the exception of regulatory quality. A positive score for institutional measures (which typically lies between -2.5 and +2.5) indicate stronger institutions while a negative score indicate weaker institutions.



Onoja et al.

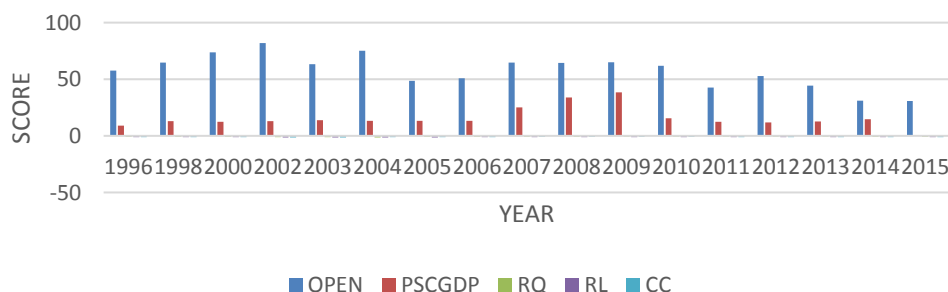
Figure 2: Trend of selected macroeconomic and institutional variables for GHANA



Source: Authors' computation using data from WDI and WGI (2015)

The data for Ghana as shown in figure 2 do not seem to agree with the trend observed for Cape Verde. While the macroeconomic variables were in the positive region for all the years under review, there is no evidence to suggest that this positive trend is accompanied by strong institutions as the institutional measures recorded negative scores during the same period. Similarly, the macroeconomic variables for Ghana appeared to be fluctuating in the positive region over the period. Arguably, the observed unstable trend may not be unconnected with the relatively weak institutions.

Figure 3: Trend of selected macroeconomic and institutional variables for NIGERIA

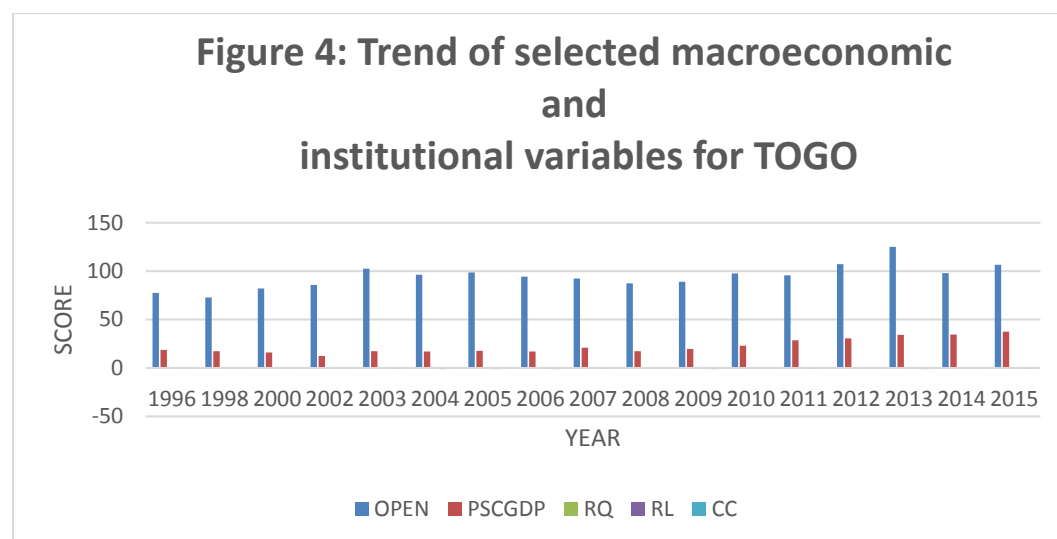


Source: Authors' computation using data from WDI and WGI (2015)



Onoja *et al.*

Trends of macroeconomic and institutional variables for Nigeria present a picture that is very similar to that of Ghana. In general, trade openness fluctuated significantly in the positive region throughout the review period. While credit to private sector was stable from 1997 to 2006, it recorded a positive trend between 2007 and 2009, and then took a downward trend in 2010. The institutional variables for the same period were in the negative region and this may be responsible for the slow growth of the macro-economic variables.



Source: Authors' computation using data from WDI and WGI (2015)

Ghana, Nigeria and Togo recorded similar patterns in trends of macro-economic variables which tend to fluctuate in the positive region over the years under review. Conversely, the trend of macroeconomic variables for Cape Verde tended to be more upward oriented indicating a better performing economy. One striking pattern observed in figures 1 to 4 is that apart from Cape Verde the other economies have institutions that are relatively weak as they all recorded scores in the negative region.

METHODOLOGY

Theoretical Framework

The theoretical framework is based on the financial deepening hypothesis proposed by McKinnon (1973) and Shaw (1973). The hypothesis sometimes referred to as complementarity hypothesis is against the notion of financial repression. The McKinnon (1973) model showed that the relationship between financial deepening and economic development is based on the complementarity between money and capital. It is assumed in this model that investment cannot be achieved without the accumulation of a significant amount of savings in the form of bank deposits, while in the Shaw (1973); model financial intermediaries witness an expansion in their activities and promote investment when savings grow higher than the level of real economic activity.



Model Specification

This study adopts with modification, the model by Baltagi *et al.* (2008) for the empirical analysis by incorporating the indicator for institutional performance in equation (1). Using annual data for estimation purposes necessitate making an allowance for the possibility that the annual observations on financial development may not represent long run equilibrium values in any given year, because of slow adjustment to changes in other variables. To allow for the possibility of partial adjustment, the study specifies a dynamic GMM model for financial development which includes a lagged dependent variable. Thus, equation (1) presents a dynamic equation for financial development.

$$FD = f(RGDPC, FDI, OPEN, INS) \quad (1)$$

The explicit form of the equation (1) is provided below

$$FD_{it} = \lambda_{11i} + \lambda_{12i}FD_{t-1} + \lambda_{13i}RGDPC_{it} + \lambda_{14i}FDI_{it} + \lambda_{15i}OPEN_{it} + \lambda_{16i}INS_{it} + \varepsilon_{it} \quad (2)$$

$i=1, 2, 3, \dots, 15$ (countries); $t=1, 2, 3, \dots, 17$ (years)

These variables are expected on apriori grounds to be signed as follows

$$\lambda_{11}, \lambda_{12}, \lambda_{13}, \lambda_{14}, \lambda_{15}, \lambda_{16} > 0$$

Three governance indicators namely, Regulatory Quality, Rule of Law and Control of Corruption were used to proxy institutions. The main explained variable is the financial development (FD_{it}) while the explanatory variables include, per capita GDP, capital inflows indicator (FDI_{it}), trade openness indicator ($OPEN_{it}$) and institutions (INS_{it}).

Model Estimation Technique

System GMM Developed by Arrellano and Bover (1995) and Blundell and Bond, (1998) was used in this work, it is considered superior to difference GMM, Bond *et al* 2001, argue that this method is able to correct unobserved country heterogeneity, omitted variable bias, measurement error and potential endogeneity.

The 15 ECOWAS countries were included for the period 2000 to 2015. The sampled countries include: Benin, Burkina Faso, Cape Verde, Cote D'Ivoire, Gambia, Ghana, Guinea, Guinea Bissau, Liberia, Mali, Niger, Nigeria, Senegal, Sierra Leone, and Togo. The period chosen was based on data availability for the chosen variables.

Table 1 Variable Definitions and Source

Variable	Identifier	Definition	Source
Broad money(% of GDP)	FD_{it}	Broad money(M2) measured as percentage of domestic product	WDI
Per capita real GDP	$RGDPC_{it}$	Real Gross Domestic product divided by population	WDI
Foreign Investment (net inflows % of GDP)	CIF_{it}	Foreign direct investment are the net inflows of investment to acquire lasting management interest I an enterprise operating in an economy other than that of the investor.	WDI



Onoja et al.

Trade(% of GDP)	TO_{It}	Sum of exports and imports of goods and services measured as a share of gross domestic product.	
Institutions	INS_{It}	<p>We applied three governance indicators to capture institution they Regulatory Quality, Rule of Law and Control of corruption</p> <p>Regulatory Quality; the ability of the government to formulate and implement sound policies and regulation that permit and promote private sector development.</p> <p>Rule of Law; the extent to which agents have confidence in and abide in the rules of the society.</p> <p>Control of Corruption is the extent of corruption and the extent to which public office are misused for private gains.</p>	WGI

Source: Author's computation

RESULTS AND DISCUSSION OF FINDINGS

The results of the study and their discussion are presented in this section. The parameter estimates were first subjected to various economic and econometric tests to ensure their validity.

Table 5.1: The Estimated Results

Dependent variable: FD			
	SGMM	SGMM ⁺	FIXED EFFECT
Fd(-1)	0.8813* (24.37)	0.8644* (12.5)	0.8951* (24.96)
Rgdpc	0.0008** (2.22)	0.0274 (1.11)	0.0001 (0.12)
Fdi	0.0345** (2.03)	0.0159 (1.09)	0.0594** (2.72)
Open	0.0190** (2.35)	-0.7422 (1.96)	0.0293* (3.35)
Rq	-1.1422 (-0.90)	2.0177 (-0.47)	-2.681** (-2.70)
Rule	3.1137* (3.40)	-0.5923 (1.83)	2.1353 (1.75)
Cc	-0.9529 (-1.16)	3.2996 (-0.52)	-1.1198 (-0.95)
_cons	3.3555** (2.34)	0.8644 (1.82)	0.7378 (0.31)



Onoja et al.

sigma_u	-	-	2.5351
sigma_e	-	-	3.6837
Rho	-	-	0.32139

Sargan test of overid. restrictions: $\chi^2(3) = 0.58$ Prob > $\chi^2 = 0.901$

(Not robust, but not weakened by many instruments.)

Hansen test of overid. restrictions: $\chi^2(3) = 0.50$ Prob > $\chi^2 = 0.919$

(Robust, but can be weakened by many instruments.)

Notes: *indicates one percent level of significance

** indicates five percent level of significance

SGMM* indicates SGMM results for ECOWAS without Nigeria

To avoid over identification, the rule of thumb is that the number of instruments must be less than or equal to the number of groups in the regression (Barais et al 2003). We can therefore conclude the absence of over identification in this study as the number of instruments is less than the number of groups ($10 < 15$). As suggested by Arrellano and Bond (1991), Arrellano and Bover (1995) and Blundell and Bond (1998), two specifications are used to test for validity of SGMM results, firstly, Sargan/Hansen test of over identifying restrictions which test for overall validity of instruments, the null hypothesis of this test states; that all instruments as a group are exogenous, therefore higher p-value is better (insignificant), the related p-value for the Sargan test statistic for instrument over-identification must be ≥ 0.05 . In this study, Sargan test of overid is 0.919, therefore the conclusion is that the instruments are not over-identified.

AR(1) and AR (2) examines whether the transformed equation is serially correlated at first and second order. It examines the null hypothesis that error term of the differenced equation is serially not correlated particularly at the second order AR(2). One should not reject the null hypothesis of this test when AR (2) is ≥ 0.05 . In this study, since AR (2) = 0.383, we cannot reject the null hypothesis. We therefore accept that the error term of the differenced equation is serially not correlated particularly at the second order AR (2). The confirmation renders the result from this study relevant and reliable for inference.

Given a t-statistics of 24.37 and a related p- value of 0.0000, the variable FD_{t-1} is evidently statistically significant at 1 percent level of significance, this is in line with the expectation of this study as we expected that past levels of financial development will affect the current level of financial development within the ECOWAS region, the positive sign of the variable is also in line with the *a priori* expectation of this study.

The positive sign on the estimated coefficient of real GDP per capita is consistent with theory as greater output is expected to improve financial development, the coefficient is also statistically significant at 5percent level of significance with t-statistics of 2.22 and related p-value of 0.043, in a more definitive term, a one hundred percent increase in the size of real GDP per capita explains about 0.084 percent of



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Onoja et al.

the increase in financial development across the study group. Therefore it is expected that as GDP per capita increases, it will lead to improved financial development of the ECOWAS region.

The sign and magnitude of the financial development indicator show that when considering financial development of the ECOWAS region, financial openness can be regarded as an important explanatory factor. As a matter of fact, financial development will improve with increased financial openness. This is because interaction with the rest of the world tend to bring international best practices to the ECOWAS region, also increased capital inflow will aid financial sector in performing some of its functions like facilitating trading, diversification and risk management, mobilizing and pooling savings and providing finance for investments, financial development thus becomes a pro-financial development tool for economies in the region, also capital inflow in the form of foreign direct investment comes with advantages like technology that might enhance the use of diversified financial instruments thus enhancing financial development in the region. With a t-statistics of 2.03 and related p-value of 0.062 the variable is both statistically significant at 10 percent level as well as economically significant in line with the expectation of this study. This result is consistent with the result of Rajan and Zingales (2003) analysis based on a panel data of twenty four industrialized countries over 1913-1999, their result suggest that opening of trade and capital accounts holds the key to successful financial development.

The trade openness indicator is positively signed, also with t-statistics of 2.35 and p-value of 0.034, it is both statistically significant at 5 percent level as well as economically significant. This result agrees with the prediction in this study as we expected that trade openness will improve financial development of the ECOWAS region, the reason for this is similar to the explanation provided for financial openness as interaction with the rest of the world brings about exposure thus making businesses to seek practices that are in tandem with practices all over the world, also increased trade will also mean increased bank balances thus enabling banks to grant more loans therefore improving access to credit. This result also agrees with the results of the study by Do and Levchenko (2004) where it was found that openness to trade will affect demand for external finance and thus financial depth in trading countries.

The results for institutions show that some institutional measures within ECOWAS are of greater economic significance than the others, results from this study show that on the average, regulatory quality will lead to a decrease in financial development in the region as the indicator of the variable carries a negative sign, with t-statistics of -0.90 and related p-value of 0.382 respectively. This contradicts the expectations of this study as we expected that improved regulatory quality will also lead to an improvement in financial development within ECOWAS. On the other hand, rule of law has a positive relationship with financial development and is statistically significant with t-statistics of 3.40 and related p-value of 0.004 thus confirming the expectation of this study that institution will have a positive relationship with financial development in the region, same can't be said of the control of corruption variable as the variable just like the regulatory quality variable has a negative sign and is statistically not significant with t-statistics of -1.16 and related p-value of 0.266 indicating control of corruption does not lead to an improvement in financial development within the ECOWAS region, rather, increased control of corruption will result in a decrease in the level of financial development in



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Onoja et al.

the region. This result contradicts results of previous studies for example Law & Azman-Saini (2008) using banking sector and stock market development indicators explored the importance of a wide range of institutional quality variables as sources of financial development and concluded that the quality institutional environment has positive effect on financial development.

Despite the fact that institutions are supposed to enhance financial development, the case for ECOWAS is different, a number of reasons may be responsible for this, in the case of control of corruption, the approach to controlling corruption might be faulty, also institutions are not strengthened to control corruption rather the process is individualized and thus the process changes as government changes. Institutions for control of corruption should be strengthened so that it depends less on individuals that way by default people will know what is expected of them. With control of corruption being highly dependent on individuals, controlling corruption might mean financial practices not being free as they used to be, in such situation as control of corruption increases it will result in a decrease in the level of financial development, the same thing applies to regulatory quality stricter regulations may slow down financial development.

Following the works of Osabuohien and Efobi (2014), sensitivity checks are conducted to determine the consistency of the result from the SGMM. The first check is done exclusive of Nigeria from the sample of countries included in the study. The main reason for this check is due to the economic size of Nigeria in the region. As it is, Nigeria's economic size is more than 57 percent of the entire ECOWAS' economy (World Bank, 2010) and this infer that their presence in the composition of the sample will likely affect the result. Of course, as expected, excluding Nigeria from the estimation affects our estimation results but the results remained valid and reliable.

The lag of the dependent variable still has a positive and is highly significant with t-statistics of 12.15 and related p-value of 0.0000, confirming that past level of financial development affects its current level, per capita GDP although maintaining its positive sign is no longer statistically significant, the level of output in this case may be too little to have any significant effect on financial development thus, the trade openness and financial openness indicators also maintain a positive sign confirming our SGMM results and the expectations of this study, two of the three institutions indicator (regulatory quality and control of corruption) maintain the signs they had in the SGMM result, rule of law was previously positively indicating that the more entrenched the rule of law is the better the financial development exclusion of Nigeria from the analysis resulted in a negative sign for the estimated coefficient of rule of law this suggest that rule of law is not as entrenched in other ECOWAS countries as it is in Nigeria. This result shows that the dominant presence of Nigeria in our analysis affects the result of estimation. The consistency in the signs confirms the findings and submissions of our earlier result.

The second sensitivity test is done to check the effect of alternative estimation technique. Using the fixed effect panel regression method, the result of this estimation technique is shown in column 4 of Table 5.1. The variables maintained the same sign as in earlier results, the lag of the dependent variable



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Onoja et al.

is still highly statistically significant as well as economically significant confirming that past levels of financial development affects its current level, real GDP Per capita remains positively related to financial development confirming that output is positively linked to financial development and this is in line with theory. The capital inflows indicator has t-statistics of 2.72 and related p-value of 0.017. This validates our earlier findings that when considering financial development of the ECOWAS region, financial openness is an important factor, it is statistically significant at the 5 percent level. The same can be said of trade openness as the indicator maintains its positive sign and is still statistically significant, thus confirming the expectation of this study. This means that as trade openness increases, financial development will also increase, in a more definitive term, on the average and across countries, a 100 percent increase in trade openness will result in about 29 percent change in financial development in ECOWAS. The signs and significance of the indicators of institution (regulatory quality, rule of law and control of corruption) are similar to signs obtained in the SGMM results. The regulatory quality and control of corruption indicators remain negatively signed and not significant while the rule of law indicator though not significant, maintains its positive relationship with financial development.

CONCLUSION AND RECOMMENDATION

The main result of this study shows that trade and financial openness contribute positively to financial development in ECOWAS, the econometric estimation result shows them to be statistically and economically significant, thus both are important when considering financial development in the region, contradictorily, institutions in ECOWAS do not contribute positively to financial development as regulatory quality and control of corruption negatively affect financial development in the region.

The study concludes that trade openness is an important factor for improved financial development in ECOWAS. Trade in the region seems to be one sided as most of the countries in the region and in Africa at large are highly import dependent and produce very little. Governments in the region should therefore put in place policies that encourage production and export, this will lead to further interaction with the rest of the world, thereby exposing countries in the region to international trade practices and increase in capital inflows from trade which will in turn improve financial development. Also, financial openness is also very essential for financial development in ECOWAS, the governments of the countries in this region should make the region attractive to foreign investors thus electricity, transport facilities and other infrastructures needed to attract investors should be put in place, that way there will be more investors which in turn will mean higher capital inflows and of course an improved financial sector. Policy emphasis should be directed at improving the quality of institutions in ECOWAS, institutions should be strengthened to control corruption, the process should not be highly dependent on individuals, thus there should be laid down rules that will not change as government changes, so that by default everyone knows the right thing to be done.

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